

This letter discusses nexus issues related to the placing of advertisements by a retail operation that has nexus in Illinois in the mail-order catalog of its out-of-State subsidiary that has no physical presence in Illinois. (This is a GIL).

March 8, 2000

Dear Xxxxx:

This letter is in response to your letter dated January 26, 2000. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

This is a request for a general information letter ruling under the provisions of 2 Illinois Administrative Code Section 1200.110 on behalf of ABC, Co. and XYZ, Co. who are clients of FIRM.

ABC, Co. and XYZ, Co. are not presently under audit by the Illinois Department of Revenue, and there is no pending litigation with the Department.

**Facts:**

ABC, Co. is a wholly owned subsidiary of XYZ, Co. XYZ, Co. is a retailer with stores located in several states throughout the United States including Illinois. ABC, Co. is a mail order seller of consumer goods. XYZ, Co. operates a separate and distinct retail business from that of ABC, Co.

ABC, Co sells to customers located throughout the United States including Illinois. ABC, Co. operations are located exclusively in STATE1 and STATE2. ABC, Co. solicits sales exclusively via: (1) mail through its catalogs, that are distributed through out the United States by either the U.S. postal service or by common carrier; or (2) ABC, Co.'s Internet website. ABC, Co. does not employ any sales persons or independent representatives to solicit sales in Illinois. ABC, Co.'s website server is located in STATE3.

ABC, Co.'s sales orders are exclusively taken, accepted and processed in STATE1 or STATE2. ABC Co. receives its orders through the U.S. postal service, telephone, and its Internet website. ABC, Co.'s products are warehoused exclusively in either STATE2 or STATE1. All merchandise returns are effectuated exclusively by the customer returning the item(s) to ABC, Co.'s STATE2 or STATE1 locations via U.S. postal service

or common carrier. No return is considered accepted until the item subject to the return is received and verified by either ABC, Co.'s STATE2 or STATE1 location.

ABC, Co. has no physical presence in Illinois. ABC, Co. has no employees, agents, or independent contractors soliciting business on its behalf in Illinois. ABC, Co. has no office, or any real or personal property in Illinois.

ABC, Co.'s retail activities are totally autonomous from XYZ, Co. However, ABC, Co. pays XYZ, Co. for internal administrative services, such as accounting services and computer services. ABC, Co. is charged arm's length fees by XYZ, Co. for these services. All services provided by XYZ, Co. for ABC, Co. are provided exclusively in STATE2 and STATE1.

To maximize economies of scale, ABC, Co. may purchase some of its products from XYZ, Co. at arm's length pricing pursuant to a non-exclusive Distribution Agreement. Products purchased from XYZ, Co. are stocked exclusively in STATE1 and STATE2. All accounts between XYZ, Co. and ABC, Co. are settled and the requisite documents, such as invoices and checks, are issued on a monthly basis.

XYZ, Co. does not solicit sales or otherwise act on behalf of ABC, Co. in Illinois or in any other state. In fact, ABC, Co. and XYZ, Co. business activities have been designed to be separate and distinct. ABC, Co. and XYZ, Co. have expended substantial time, energy and costs to carefully operate their respective businesses autonomously. Customers deal with the companies on a separate basis. XYZ, Co. does not accept or effectuate any order, delivery, payment or return of merchandise on behalf of ABC, Co. Merchandise purchased from ABC, Co.'s catalog or website cannot be returned at XYZ, Co.'s retail stores. ABC, Co. does not display any signage or distribute its catalogs in any of XYZ, Co.'s retail establishments. Customers may not place an order or contact ABC, Co. from XYZ, Co.'s retail establishments.

A portion of ABC, Co.'s revenue is received through advertisements in its mail order catalog. ABC, Co.'s catalogs contain paid advertisements from ABC, Co.'s suppliers. In essence, ABC, Co. sells advertising space in its catalogs to its suppliers, upon which ABC, Co. charges a fee.

XYZ, Co. is contemplating placing advertisements in ABC, Co.'s mail order catalogs comparable to other ABC, Co.'s vendors' placement of advertisements in ABC, Co.'s catalogs. The transaction would be priced at arm's length.

**Authority:**

The United States Supreme Court has established the minimum requisite presence for sales and use tax nexus. Pursuant to the Court's findings in Quill Corp. v. North Dakota, 112 S.Ct. 1904 (1992) and National Bellas Hess, Inc. v. Department of Revenue, 386 U.S. 753 (1967), the Court has determined that sales and use tax nexus

exists only when it has been determined that a potential taxpayer has substantial physical presence in a state.

Courts that have addressed the issue have held that the physical presence of a discrete corporation cannot be attributed to a separate out-of-state seller. See, e.g., *SFA Folio Collections, Inc. v. Bannon*, 217 Conn. 220, cert. Denied, 111 S.Ct. 2839 (1991); *Bloomington's by Mail, Ltd. v Commonwealth Department of Revenue*, 591 A.2d 1047 (Pa. 1991); *Current, Inc. v. California Board of Equalization*, 24 Cal. App.4<sup>th</sup> 382 (1994).

This U.S. Constitutional standard has been specifically addressed by Illinois in its Private Letter Ruling ST 95-0347 (Aug. 15, 1995). This Ruling determined that a taxpayer did not have substantial nexus with Illinois resulting from the activities of its corporate affiliates. The ruling was determined based on the taxpayer's representations that it did not have physical presence in the state. The taxpayer, a mail-order company, was engaged in the business of selling fitness equipment and related products throughout the United States by catalogs, brochures and national advertising media.

The taxpayer had no employees, representatives, independent contractors, or agents operating in Illinois under its authority. Furthermore, the taxpayer had no sales office, retail store, or any other real or personal property in the state. However, a wholly owned subsidiary of the taxpayer operated retail stores and kiosks in Illinois. The subsidiary's product line was similar to that of the taxpayer. The subsidiary purchased some of its product line from the taxpayer pursuant to a non-exclusive Distribution Agreement. Additionally, the subsidiary purchased administrative services from the taxpayer. All transactions occurred outside of Illinois and the fees charged were at arm's length.

The ruling determined that the subsidiary's nexus with Illinois did not create Illinois use tax nexus for the taxpayer. The transactions conducted by the taxpayer to the subsidiary did not create an agency relationship in Illinois.

### **Taxpayer s Position:**

Pursuant to the United States Supreme Court case law, decisions in other State Courts and the Illinois Private Letter Ruling, ABC, Co.'s proposed advertising transaction with XYZ, Co. does not create substantial physical presence in Illinois for ABC, Co. Neither ABC, Co.'s business activities nor its business relationship with XYZ, Co. create use tax nexus for ABC, Co. in Illinois. Under the facts presented, neither entity is the alter ego or agent for the other.

### **Ruling Requested:**

Based on the facts presented above, XYZ, Co.'s advertisements placed in ABC, Co.'s mail-order catalog will not create sales or use tax nexus for ABC, Co. in Illinois for purposes of Illinois sales and use tax under an agency, affiliate or other theory. Illinois

law does not require ABC, Co. to register as a vendor and collect Illinois sales or use tax in the state on its mail order or Internet sales.

If you anticipate issuing a General Information Letter which does not agree with the ruling requested, I would appreciate the opportunity to meet with you to discuss the issues in greater detail before a ruling is issued. I request that the names of the parties be deleted from any public publication of the letter and that all documentation submitted with the letter be held as confidential information.

Please call me at #### if you have any questions.

Determinations regarding sales tax nexus are normally very fact specific. We cannot make a binding determination on this issue in the context of a General Information Letter. However, the following discussion may be helpful for businesses to use in determining their Illinois tax liability.

The Department agrees that the XYZ Co. advertisements placed in ABC Co.'s mail-order catalog do not create nexus for ABC Co. in Illinois for purposes of Illinois sales and use tax. This is based upon the representation that ABC Co. has no physical presence in Illinois. ABC Co. has no employees, agents, or independent contractors operating in Illinois under its authority. ABC Co. has no office or any real or personal property in Illinois. While ABC Co. is a wholly owned subsidiary of XYZ Co., which does have nexus in Illinois, it is the Department's understanding that XYZ Co. does not serve as a representative or agent for ABC Co. in Illinois.

ABC Co. and XYZ Co. are organized as separate and distinct entities. They have no integrated operations or management. All transactions between the two companies are conducted on an arm's length basis. This includes the provision of internal administrative services such as accounting and computer services by XYZ Co. for ABC Co., at a location outside of Illinois, and the purchase of products by ABC Co. from XYZ Co., under a non-exclusive distribution agreement and wherein the products are stocked outside of Illinois. The placing of XYZ Co.'s advertisements in ABC Co.'s mail-order catalog, also accomplished on an arm's length basis, does not create nexus in Illinois for ABC Co. for purposes of sales and use tax.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at [www.revenue.state.il.us](http://www.revenue.state.il.us). If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

ST 00-0043-GIL

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